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Letter dated 13 June 2005 from the Secretary-General addressed to the President of the Security Council

Pursuant to Security Council resolution 1483 (2003), I have the honour to transmit the attached letter from my representative on the International Advisory and Monitoring Board for Iraq (see annex). It contains updated information on the Board's activities and follows his letter of 6 January 2005 (S/2005/12, annex).

I should be grateful if you would bring this letter and its annex to the attention of the members of the Security Council.

(*Signed*) Kofi A. **Annan**

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Annex

[Original: English]

Letter dated 2 June 2005 from the representative of the Secretary-General on the International Advisory and Monitoring Board for the Development Fund for Iraq addressed to the Secretary-General

As your representative on the International Advisory and Monitoring Board (IAMB) for the Development Fund for Iraq, I am pleased to provide you with an update on the activities of the Board since my letter dated 6 January 2005, in which I recapped the actions of IAMB during 2004.

IAMB received, on 21 May 2005, the audit reports by KPMG covering the audit of Iraq's oil export sales and Development Fund for Iraq operations for the period stating with the dissolution of the Coalition Provisional Authority on 29 June 2004 and ending on 31 December 2004. The reports were immediately posted on the IAMB website (www.iamb.info) and a press release was issued.

The audit reports consist of the statement of cash receipts and payments for the Development Fund for Iraq for the period from 29 June to 31 December 2004 and the following reports: report of factual findings in connection with export sales; report of factual findings in connection with the oil proceeds receipts account; report of factual findings in connection with disbursements; and management letter on internal controls.

The audit reports continue to be critical of the controls in place in the spending ministries, the United States agencies in respect of the outstanding commitments using Development Fund for Iraq resources and the Iraqi administration of Development Fund resources. The main weaknesses include: (a) incomplete Development Fund accounting records; (b) untimely recording, reporting, reconciliation and follow-up of spending by Iraqi ministries; (c) incomplete records maintained by United States agencies, including disbursements that were not recorded in the Iraqi budget; (d) lack of documented justification for limited competition for contracts at the Iraqi ministries; (e) unreconciled quantities of oil and oil products exported, indicating a lack of control and possible misappropriation of oil revenues, and significant difficulties in ensuring completeness and accuracy of Iraqi budgets and controls over expenditures; and (f) the non-deposit of proceeds of export sales of petroleum products into the appropriate accounts in contravention of Security Council resolution 1483 (2003).

IAMB had the opportunity to review those reports in draft form with the auditors at its meeting on 17 and 18 April.

IAMB decided to draw to the attention of the Government of Iraq the weaknesses identified in the audit reports and to invite the Government to act on the audit recommendations to strengthen the financial controls and the administration of the Development Fund for Iraq.

Modalities are currently being explored to extend the audits to cover the period from 1 January to 30 June 2005.

IAMB also followed up on the recommendations made in the context of previous Development Fund audits and requested a briefing by the interim Government of Iraq on steps taken to address the concerns that were raised by IAMB in the light of the findings contained in the two previous audits of the Development Fund covering the period from May 2003 to June 2004.

At the meeting held in April, the member representing the interim Government of Iraq provided information on the steps that were being taken to strengthen controls in the Ministry of Oil, including: (a) installation of an integrated computer system; (b) inspection and certification of imported oil products; (c) completion of feasibility studies on oil metering; and (d) the issue of an invitation to tender for a comprehensive oil metering system. Steps have also been taken to strengthen controls at spending ministries, including: (a) scheduling the implementation of a comprehensive financial management information system by 2007; (b) implementing procedures, in coordination with the Board of Supreme Audit, over receipts, payments and procurement; (c) scheduling an audit of all contracts concluded in 2003 and 2004; (d) appointing inspectors general in all Iraqi ministries; and (e) establishing an integrity commission to look into financial irregularities and abuse.

IAMB was briefed on measures taken to control the disbursements from the Development Fund for Iraq, including the closure of current accounts at various ministries and the establishment of a procedure whereby allocated funds would not be transferred to the ministries but disbursements to the ministries would be based on estimated monthly needs.

IAMB also received a briefing from the Iraq Board of Supreme Audit. The President of the Board noted the difficult task the Board was facing and pointed out that the adoption of the public debt and financial administration law would assist in the administration of funds. He also indicated that the creation of a contract management capacity in each ministry was being considered. The Board is planning to widen its audit coverage at the State Oil Marketing organization. With regard to smuggling, the Board intends to submit a report to the Council of Ministers on the control procedures that could help to address this matter.

In my previous letter, I had informed you that IAMB had agreed to the terms of reference for a special audit of sole-sourced contracts using Development Fund for Iraq funds proposed by the United States Government, to be completed by an independent auditor. In a letter dated 15 April 2005, the United States Government informed IAMB that an auditor had been selected. The special audit of sole-sourced contracts calls for: (a) identifying all contracts awarded non-competitively by the Coalition Provisional Authority valued at over $5 million that used Development Fund funds; (b) providing a summary of the findings of audits of such contracts that have already been conducted by various United States Government audit agencies; and (c) conducting additional audit procedures on non-competitively awarded contracts that have not been the subject of audit, including whether such contracts were consistent with the purposes outlined in Security Council resolution 1483 (2003).

IAMB has been briefed by a representative of the United States Department of Defense, who provided additional clarifications regarding the status of the audit. The audit reports are scheduled for completion and transmission to IAMB by the end of August 2005.

IAMB took note of the report of the Special Inspector General for Iraq Reconstruction dated 30 January 2005 regarding the oversight of funds provided to Iraqi ministries through the national budget process. IAMB noted that the findings contained in the report were along the same lines as those identified in the Development Fund for Iraq audits carried out fo. the IAMB.

IAMB noted that the unredacted Defense Contract Audit Agency reports covering sole-sourced contracts had been made public. Those reports refer to overcharges and questionable amounts billed under the sole-sourced contracts of an amount in excess of $200 million. IAMB noted with regret that those findings had been redacted in earlier reports of the Agency submitted to IAMB.

The next meeting of IAMB is tentatively scheduled for September. By that time, the special audit of sole-sourced contracts using Development Fund for Iraq funds should be available, as should the audit of the Fund covering the period from 1 January to 30 June 2005.

(*Signed*) Jean-Pierre **Halbwachs**
Representative of the Secretary-General to
the International Advisory and Monitoring Board